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# You don't need to be a lefty to support Krugman

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By Samuel Brittan

The remedy for too little spending is more spending. Everything else is commentary.

This is the moral I draw from Paul Krugman's *End This Depression Now!* Although it is not without flaws, I hope without much confidence that the book's wide readership includes the UK prime minister and chancellor.

Mr Krugman follows Keynes's definition of a depression as "a chronic condition of subnormal activity without any marked tendency either towards recovery or towards complete collapse". Can anyone doubt whether this – or worse – is the condition of many western economies? With the exception of Canada, output in the G7 countries is still no higher than at its 2007-2008 peaks. In the UK and Italy it is now 4-6 per cent below those peaks.

It is difficult to imagine Mr Krugman cheering for the Republicans. Nevertheless I cannot sufficiently emphasise that there is nothing essentially "leftwing" about his analysis. Consumers will not spend because of a backlog of indebtedness and businesses will not invest because of pessimism about market prospects. Central banks can inject money, but there is a limit to what they can do when nominal interest rates are near zero. The Bank of England's "no change" decision on Thursday illustrates these limits as well as the native caution of most central banks. This leaves governments to fill the gap.

Where will they get the money from? Governments of countries that have the good fortune to run their own currencies can borrow as much as required whether directly or indirectly from their central banks. But won't this "printing of money" be inflationary? Yes, in normal times. But not when there is an ever-widening pool of unemployed people and of unused capacity.

I wish there were a way of getting finance ministers to learn by heart the chapter on the folly of their deficit obsession. As Mr Krugman says: "The government is simply finding a use for the excess of what the public wants to save over what it is willing to invest." And if they find that too abstract they should at least take account of the repeated falsification of the fears of US bond vigilantes. We have suffered enough from the urge to make economic policy a morality play.

There is nothing new about the hostility of conventional opinion to the Krugman message. Keynes faced similar hostility when he tried to rescue capitalism from the Depression. He

regarded his *General Theory* as “moderately conservative in its implications” and consistent with an economy run on private enterprise principles.

Why has this message been so difficult to accept? There is always the doctrine of “unripe time”. Speak to any member of the British cabinet at random and I am sure you will hear of the folly of undertaking experiments when the eurozone is on the brink of collapse.

But why then are the leaders of the eurozone so reluctant to rein back the restrictionist policies, something that might – just might – save the currency from complete collapse? Mr Krugman believes there is an underlying explanation: “Concede that government can play a useful role in fighting slumps and the next thing you know we’ll be living under socialism.”

But I have a simpler explanation. A shopkeeper or private citizen who cannot make ends meet is unlikely to get out of his debts by borrowing more. These truisms are then wrongly applied to governments: a long-established logical error known as “the fallacy of composition”.

No book is perfect and I have two reservations about Mr Krugman’s. The first is the emphasis on boosting government spending. Now, when real interest rates are low or negative, is indeed an ideal time to undertake infrastructure projects. Nevertheless, demand could just as well be expanded by the tax-cutting route. Would tax cuts be spent? Yes, if they are aimed at lower-income families or if they are VAT cuts announced as temporary. Too much emphasis on public spending reinforces the erroneous impression that expansionist policies are a “big government” idea.

I have a stronger objection to Mr Krugman’s proposal to raise national inflation targets from 2 per cent to 4 per cent. At a stroke the real burden of debts would be slashed. A similar suggestion is made by a notable British economic historian, Nicholas Crafts, in a paper for the liberal think-tank CentreForum that cites the avowed aim of raising prices by an earlier Conservative-dominated coalition from 1932 onwards.

But that government was starting from a background of stable or even falling prices, whereas governments in the past few decades have been struggling to prevent creeping inflation from degenerating into the runaway variety. Apart from anything else, who would now believe any official reassurance that the target would not be raised again?

None of these reservations, however, detracts from Mr Krugman’s thesis. It should be read on the basis of its evidence, not on its alleged ideological baggage.

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